

SECRET

3

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PRIME MINISTER

Community Budget

The paper we have prepared for Wednesday's discussion sets out the questions to be considered in deciding what might or might not be an acceptable outcome at Dublin. You will wish to take the meeting through them and hear what the others present think. The Chancellor of the Exchequer has probably got his sight set on a reduction of between two-thirds and three-quarters, but will be especially concerned to ensure that we do not make another mistake and that this time the solution should be sufficiently robust to be certain of working in any foreseeable circumstances. The Foreign and Commonwealth Secretary may be more inclined to settle for, say, a half now with promises about a further reduction in the future. You will have your own views, and you need not necessarily reveal at this meeting precisely what your own sticking points will be: another meeting just before Dublin may be necessary (especially as the Chancellor will not be at Dublin). But you will need to decide in the light of this meeting what is and is not likely to have the support of your colleagues; and how much and when to tell your colleagues in Cabinet of your intentions.

2. The gap between our minimum requirements and what the French and others are willing to concede will be big. We shall probably be offered a new Financial Mechanism, but much may turn on the question whether the Community can adapt existing mechanisms to give us what we need, or whether we have to seek to be directly compensated for our low receipts. Only the Belgians have so far shown any disposition to go that far: reluctance on the part of the rest will be strong and deep-rooted. One possibility which has been mooted but is not dealt with in the paper is some kind of special fund or lump sum for a specific project or projects of benefit to the United Kingdom. Whether, if offered, this would be worth looking at would depend on how big the sum was; for how long it would be available; and whether it could be tied in with existing rather than new public expenditure. We do not have to rule this out; our partners may well be reluctant to propose it.

SECRET

3. Even if the prospects for a successful outcome in Dublin are uncertain, it would be wrong to conclude now that we shall fail. No-one is in any doubt about your determination and other Governments will only now be seriously applying their minds to how far they are really prepared to go. One of the features you may like to raise is the problem of how little we appear to have to offer in return. We do not need to negotiate on the budget other than on its merits, or to see it as part of a bargain; but we have to face the reality of the fact that other Governments will have to justify to their Parliaments and public opinion giving something up in our favour. To do that, they will need to point to something they have got out of us. This Government has already had to promise a more constructive European commitment to get even as far as we have. On the specific issues, you ruled out at your meeting on 17th October saying anything on EMS. But I wonder whether you should not reconsider including some words in the Dublin communique of the kind you have already used publicly i. e. that it is the Government's objective to join EMS but that the timing will need to be a matter for discussion with our partners. On the CAP, you could subscribe to its importance for the Community while still criticising the surpluses (we shall still have the 1 per cent VAT ceiling as a means of holding down the cost). You will not want to have fisheries brought up at Dublin but you may be pressed bilaterally by Giscard to guarantee historic rights for his Breton fishermen. And he may need your help on sheepmeat. As you know, OD(E) has been looking at the energy card but so far has not come up with anything of real positive merit. This is partly out of a natural desire to safeguard our own position first, and partly because of the difficulties that would be caused with the Americans and the Japanese if we gave the rest of the EEC preference over other IEA countries. With developments in Iran, the rest of the Community will be more worried than ever about prices and security of supplies. Unless we can show some understanding, we shall have North Sea oil thrown at us as a reason why we should shoulder the budget burden.

4. If it becomes clear that no solution in Dublin is possible, OD has agreed that the next step would be to insist on another early meeting of the European Council. This would be unprecedented, and would certainly mark the seriousness of the crisis. You would need to make it clear that, so far as we were concerned, the rest of the Community's work would be in suspense; so the sooner the

SECRET

European Council reconvened, the better. There might be a disposition to invite, say, Mr. Lynch and Mr. Jenkins to search for an acceptable compromise in the meantime: we could hardly object. The important thing would be to keep up the pressure. The others will not relish the prospect of a prolonged crisis, and nor should we. Even if the TNF has gone well at the NATO Council, we shall not want to see Western Europe preoccupied with an internal crisis. The Soviet Union will be only too ready to exploit such a situation. And the closer we get to the German and French elections, the harder it will be for them to move.

5. This suggests that our tactics should be directed at getting a solution if possible before the end of the year but at least as early in 1980 as possible. It would be understood by our partners, even if unwelcome to them, that during this period we would be unco-operative. There are Council meetings on research and transport in early December. We could stop anything being settled. We could, if we so wished, prevent the Community adopting any further mandates for negotiations with Spain and Portugal (although that would lead to pressure on us from those countries). We would not be able to prevent the adoption of the 1980 budget and if we were to prevent progress on fisheries we risk running up against adverse rulings from the Court. Blocking decisions to regulate the steel industry in 1980 would also be against our interests. Going into 1980, we could threaten to invoke "the Luxembourg compromise" to prevent any increase in farm prices (for which the pressure next spring is likely to be greater than last time). In his OD paper, the Foreign and Commonwealth Secretary recommended a graduated response with a selective policy of obstruction. If it were agreed that we should go for an early settlement, there would be something to be said for simply blocking all forms of new expenditure from which we would not benefit.

6. Chancellor Schmidt's reaction to what you told him was that we were putting our membership at stake. Some of your Cabinet colleagues reacted in the same way. It may well be true that failure to find a reasonably satisfactory solution of the budget problem would eventually bring the question of continued membership back to the centre of the British political stage - something which our partners in the Community would like to avoid as much as the Government would. But that is a very different matter from threatening to pull out if we do not get our way. I doubt whether there would be a majority in the Cabinet for that course

SECRET

and I also doubt whether it would be very effective as a threat to our partners. So the best answer to Chancellor Schmidt (and others who may take the same line) is that Britain wants to be a good and whole-hearted member of the Community, and has no intention of leaving; and that we therefore intend to press our case from within: to sit it out and, if necessary - of course we hope it won't be - make life awkward for everyone else. When General de Gaulle was dissatisfied, he did not leave the Community but he brought it to a standstill. His empty chair tactic proved to be the wrong one: we can achieve the same result as effectively and with less risk to our own interests by remaining in our place and being as bloody-minded as we know how. This would be very vexatious for our partners, but it would be extremely difficult for them to evict us.

7. We should not however reveal any of this before Dublin. To do so would destroy any chance we might have of pocketing what is on offer at Dublin and still continuing to argue the toss over the rest.

ROBERT ARMSTRONG

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13th November, 1979